Supreme Court, U.S.
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No. 99-995

IN THE

Supreme Court of the United States

SMS SYSTEMS MAINTENANCE SERVICES, INC.,

Petitioner,

v.

DIGITAL EQUIPMENT CORPORATION,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

RESPONDENT'S BRIEF IN OPPOSITION

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LIST OF PARTIES TO THE PROCEEDING and RULE 29(6) STATEMENT

The parties to the proceedings below were petitioner SMS Systems Maintenance Services, Inc. ("SMS") and respondent Digital Equipment Corporation ("Digital"). Pursuant to Supreme Court Rule 29(6), respondent Digital states that it was acquired by and merged into Compaq Corporation in 1998. Compaq Corporation has no parent corporation and no publicly held company owns 10% or more of its shares.

TABLE OF CONTENTS

	Page
LIST OF PARTIES TO THE PROCEEDING AND RULE 29(6) STATEMENT	i
TABLE OF CONTENTS	ii
TABLE OF CITED AUTHORITIES	v
RESPONDENT'S STATEMENT OF THE CASE	1
Introduction	1
Background Facts	2
A. Warranties and Competition	2
B. Digital's Adoption of Three-Year Warranties on Certain Products and the Legitimate Competitive Reasons for That Adoption	3
C. Service and Maintenance of Computers	4
D. Procedural History	6
E. The First Circuit's Decision	7
REASONS FOR DENYING THE WRIT	9
Summary of Argument	9

Contents

Page

I. THE FIRST CIRCUIT CORRECTLY APPLIED WELL-ESTABLISHED SUMMARY JUDGMENT STANDARDS AND ITS DECISION DOES NOT CONFLICT WITH *KODAK* 10

A. The Summary Judgment Standards Are Well Established; No Important Federal Question Is Raised by Application of Those Standards to the Record Facts of this Case 10

B. The First Circuit's Decision — and Its Analysis of Section 2 of the Sherman Act — is Entirely Consistent with *Kodak* and Other Supreme Court Precedent 12

II. THE FIRST CIRCUIT RIGHTLY IDENTIFIED A NUMBER OF WAYS IN WHICH SMS FAILED TO PRODUCE SUFFICIENT EVIDENCE TO SUPPORT SEVERAL ESSENTIAL ELEMENTS OF ITS SECTION 2 CLAIM 15

A. SMS Failed to Present Evidence of the Supposed "Lock-In" 15

B. SMS Failed to Rebut Undisputed Evidence of Digital's Legitimate Business Interest in Adopting the Warranties 17

Contents

Page

C. SMS Failed to Provide Any Evidence of Another Essential Element of Its Claim: Antitrust Injury 19

III. THERE IS NO CIRCUIT SPLIT; THE FIRST CIRCUIT'S OPINION IS CONSISTENT WITH THE OTHER CIRCUIT COURT CASES ON AFTERMARKET ISSUES AND WITH *KODAK*. 20

CONCLUSION 24

TABLE OF CITED AUTHORITIES

Page

Cases:

Acosta-Mestre v. Hilton Int'l of Puerto Rico, 156 F.3d 49 (1st Cir. 1998) 16

Anderson v. Liberty Lobby, Inc., 477 U.S. 242 (1986) 10, 11, 16, 20

Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985) 18

Brown Shoe Co. v. United States, 370 U.S. 294 (1962) 14

Celotex Corp. v. Catrett, 477 U.S. 317 (1986) 10

Datagate, Inc. v. Hewlett-Packard Co., 60 F.3d 1421 (9th Cir. 1995), *cert. denied*, 517 U.S. 1115 (1996) 22

Daubert v. Merrell Dow Pharmaceuticals, Inc., 509 U.S. 579 (1993) 16

Digital Equip. Corp. v. Uniq. Digital Tech., Inc., 73 F.3d 756 (7th Cir. 1996) 23

Eastman Kodak Co. v. Image Technical Servs., Inc., 504 U.S. 451 (1992) ..... *passim*

Grappone, Inc. v. Subaru of New England, Inc., 858 F.2d 792 (1st Cir. 1988) 18

Cited Authorities

Page

Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2 (1984) 23

Kumho Tire Co. v. Carmichael, 526 U.S. 137, 119 S. Ct. 1167 (1999) 20

Lee v. Life Ins. Co. of N. Am., 23 F.3d 14 (1st Cir.), *cert. denied*, 513 U.S. 964 (1994) 6, 14

Marts v. Xerox, Inc., 77 F.3d 1109 (8th Cir. 1996) 23

Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574 (1986) 10, 11, 17

Medina-Munoz v. R.J. Reynolds Tobacco Co., 896 F.2d 5 (1st Cir. 1990) 11

Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752 (1984) 11

PSI Repair Serv. Inc. v. Honeywell, Inc., 104 F.3d 811 (6th Cir.), *cert. denied*, 520 U.S. 1265 (1997) 23

Red Lion Med. Safety, Inc. v. Ohmeda, Inc., 63 F. Supp. 2d 1218 (E.D. Cal. 1999) 22

Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447 (1993) 19

Cited Authorities

Page

Springfield Terminal Ry. Co. v. Canadian Pac. Ltd., 133 F.3d 103 (1st Cir. 1997) 10, 11

United States v. Grinnell, 384 U.S. 563 (1966) ... 13

Statutes:

15 U.S.C. § 2 ..... 1, 6

15 U.S.C. § 2301 2

15 U.S.C. § 2302(a) 2

15 U.S.C. § 2302(b)(1)(A), *et seq.* 2

Rule:

Fed. R. Civ. P. 56(e) 11

Other Authorities:

3A Areeda & Hovenkamp, *Antitrust Law* ¶ 761 (1996) 2, 15

11A Areeda & Hovenkamp, *Antitrust Law* ¶ 531 (1996) 13, 14

Niskanen, *Freedom of Contract as Tort Reform*, 1 Mich. L. & Pol'y Rev. 1 (1996) 2

RESPONDENT'S STATEMENT OF THE CASE

Introduction

This case arises out of Digital's decision, starting in 1994, to promote the sales of its new line of 64-bit Alpha computers by introducing them with a standard three-year hardware warranty. In doing so, Digital was matching the standard three-year warranty offered on competitive Compaq machines, beating the warranties of other competitors such as IBM, Hewlett-Packard and Sun Microsystems, and demonstrating to purchasers of the novel 64-bit technology that Digital stood behind its innovative product.

Petitioner SMS, a company which provides "multi-vendor" service to computers manufactured by a number of different companies, including Digital, then sued, claiming that Digital is barred by Section 2 of the Sherman Act, 15 U.S.C. § 2, from competing in the fiercely competitive computer industry by offering new products with a standard warranty that is included in the price of the product. In particular, SMS claimed that Digital's warranty constitutes an unlawful attempt by Digital to monopolize what SMS claims is the derivative aftermarket for "services relating to Digital's computers."

In a decision dated August 19, 1999 and reported at 188 F.3d 11, the United States Court of Appeals for the First Circuit affirmed a decision of the United States District Court for the District of Massachusetts (Harrington, J.), granting summary judgment against SMS's claims.[1] SMS has now petitioned this Court for a writ of certiorari to review the First Circuit's decision. For the reasons set forth below, the petition should be denied.

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1. The District Court's decision is reported at 11 F. Supp. 2d 166.

Background Facts

A. Warranties and Competition.

Automobiles. Televisions. Stereos. VCRs. Copiers. Printers. Computers. Just about every durable good comes with a warranty. Standardized product warranties have been in use by manufacturers since at least the late 1800s. Manufacturers of durable goods have long competed for customers by offering warranty terms that are the same as, different from, or better than, those of their competitors. 3A Areeda & Hovenkamp, *Antitrust Law* ¶ 761, at 55 (1996) (warranty protection is a tool of "non-price competition"); Niskanen, *Freedom of Contract as Tort Reform,* 1 Mich. L. & Pol'y Rev. 1, 4 (1996) ("Firms can and do compete with respect to warranties . . . just as well as they compete with respect to any other product characteristic . . . ."); *see also* Magnuson-Moss Warranty Act, 15 U.S.C. §§ 2301, 2302(a), 2302(b)(1)(A), *et seq.*

It was undisputed below that computer manufacturers have traditionally sold computers with standard warranties ranging from one to three years, and more for certain components. SA125, 129; SA90-91; A22.[2] For example, prior to 1994, Digital's computer products had a base-level "product foundation" warranty that was included in the price of the computer. SA484-85; SA195, 200-202. Also undisputed is that computer equipment manufacturers like Digital have vigorously competed with one another by offering longer and more comprehensive warranty protection on new equipment. SA93-104; SA318-19.

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2. The record Appendix and Supplemental Appendix on appeal are cited as "A__" and "SA__," respectively. The District Court's and First Circuit's opinions are cited as "Mem. at __" and "Op. at __," using the pagination in SMS's Petition.

B. Digital's Adoption of Three-Year Warranties on Certain Products and the Legitimate Competitive Reasons for That Adoption.

The warranties at issue in this case are three-year warranties on certain computer systems sold by Digital beginning in 1994. At that time, Digital was introducing a new line of computers — the "Alpha" computers — which were driven by Digital's innovative 64-bit Alpha chip. SA126.[3]

The computer marketplace into which the Alpha systems were introduced is highly competitive. Prospective computer customers can choose from competing machines offered by such companies as IBM, Hewlett-Packard, Compaq, Sun Microsystems and Dell; they can choose different models from Digital; they can obtain computers on the used and refurbished equipment market; or they can choose to continue to use their existing equipment. SA127, 133. The warranty terms offered with the many competing products vary not only in duration, but also in specific terms relating to speed of service and time of coverage. *Id.* SA125.

Digital provided extensive record evidence confirming that a substantial number of customers preferred three-year warranties. Industry watch dogs, including Dataquest, had reported that three-year warranties were becoming a trend that other manufacturers would follow. SA128. By 1997, a Dataquest survey found that 39% of server customers *required* a warranty of three years or more. SA87. And, a research report that SMS itself introduced below confirms that Digital customers "considered [the three-year warranty] to be standard for competitive products in the class." SA915. Digital's competitor, Compaq, in adopting its three-year warranties, independently

3. One year later, after a consumer survey conducted for Digital by an outside consultant demonstrated a consumer preference for three-year warranties, Digital also adopted a standard three-year warranty for new sales of certain updated versions of its older line of VAX computers. SA129-30; SA137-52.

concluded that consumers "generally preferred three-year warranties . . . over one-year warranties." SA4.

Digital also provided extensive evidence that it had adopted its three-year warranty for a number of legitimate business purposes: to respond to competition; to be at the forefront of the trend toward longer warranties; to differentiate its products from those with lesser warranties; to signal to customers that Digital would stand behind its products; and ultimately to make Digital's products more attractive to customers. SA126-28. As an industry analyst put it, the move to three-year server warranties was "the result of one very strong market force — competition." SA89; *see also* SA109, 114.[4]

The length of Digital's warranties, and the specific terms of the warranty (describing what was covered and what was not), were fully set forth in written materials provided to customers and were readily available through Digital and other companies who sold Digital computers. SA154-67, 266-301; SA126, 129, 131. SMS conceded that "customers are fully aware that they are paying for the three-year warranty."[5] A82.

C. Service and Maintenance of Computers.

Computer users have several choices for servicing and maintaining their computer equipment. SA169-70. Warranty service is available for computers that are under warranty. Users also have the option of doing their own service on their equipment. *Id.* And, users can obtain service from entities that provide hardware maintenance services through service contracts or on a spot basis. *Id.* There are thousands of companies

4. Digital offered its Alpha systems at a price that incorporated the three-year warranty. Digital's prices were set to compete directly with other products offered with lesser warranties. SA126; SA859-64.

5. Digital's customers could also choose to buy Alpha or VAX systems without three-year warranties through an active used and refurbished equipment market. A213-14; SA133.

— including large companies operating nationwide — capable of providing service on Digital's computers (and on those of other manufacturers) through what is widely known as "multi-vendor customer service." SA170-71; SA171-73; SA184-86A (listing over 60 companies). They include "Independent Service Organizations" ("ISOs") which are not affiliated with any particular manufacturer. SA 169-70. SMS is an ISO.

Significantly, *Digital's warranty does not limit a purchaser's ability to use service providers besides Digital* during the warranty period. While under warranty, the computer may be serviced by any other service provider — including ISOs like SMS — and Digital does not revoke the warranty or otherwise penalize a customer if it goes elsewhere for service during the warranty period. SA132; SA154-66.

SMS came forward with no evidence that Digital's adoption of three-year warranties has caused *any* harm to competition for services relating to Digital's computers. Not a single witness or affidavit stated that the warranty has caused any service company to go out of business, has resulted in an increase in service prices, or has caused a reduction in supply or quality of service for Digital machines. To the contrary, it was undisputed that SMS and other companies continue to compete and continue to offer service to all Digital users. SA13-16, 21-23; SA33, 36-38, 42-45, 51-53; SA68-69; SA172. Competition for services has continued to be robust before, during and after Digital adopted three-year warranties.[6]

6. Indeed, SMS's president and owner testified that SMS was providing service to Alpha computers even before the three years had expired since Digital introduced the three-year warranties in 1994. SA14-16. He also testified that SMS has been competing with Digital and others for service contracts as Digital's machines came off warranty. SA21-23. And he identified fifteen other companies providing service to Digital computers and competing with Digital and SMS. SA13, 29-30. SMS's president also admitted that SMS was able to hire trained technicians for Digital equipment, and that parts for Digital computers were readily available, including from Digital itself. SA19-20, 24-25, 28.

D. Procedural History.

SMS alleged in its amended complaint that Digital adopted three-year warranties in place of the previous one-year warranty in order to drive SMS and other service providers out of business by preventing them from competing for the sale of services to Digital computer users. A23-24. SMS asserted a federal antitrust count under 15 U.S.C. § 2, plus two derivative state-law claims.

The parties conducted extensive discovery, including expert reports and depositions, over more than a year. SA 56-122; SA168-86A. In moving for summary judgment, Digital presented several alternative grounds: (i) the court should assess the monopoly power issue in the context of the primary equipment market, in which SMS conceded Digital held an insubstantial share, not in the alleged aftermarket for services; (ii) SMS could not show the required "antitrust injury"; and (iii) undisputed evidence established that Digital was acting with a legitimate business purpose when it adopted its warranties.

After a hearing, the District Court granted summary judgment for Digital. Among other things, the court noted the applicability of the Supreme Court's admonition that: "It is undisputed that competition is enhanced when a firm is able to offer various marketing options, including bundling of support and maintenance service with the sale of equipment. Nor do such actions run afoul of the antitrust laws." *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 478-79 (1992) (hereinafter "*Kodak*"). Mem. at 39A. The court also found that all the circuit courts to address similar claims since *Kodak* had rejected attempts, like that of SMS, to "shoehorn their allegations into [the] *Kodak* 'derivative aftermarket' model." Mem. at 38A-42A (citing *Lee v. Life Ins. Co. of N. Am.*, 23 F.3d 14, 18 (1st Cir.), *cert. denied*, 513 U.S. 964 (1994)). The court also recognized correctly that Digital's warranties were adopted for the legitimate business purpose of promoting sales in the computer equipment market. Mem. at 39A, 42A. SMS appealed.

E. The First Circuit's Decision.

After oral argument, the First Circuit entered its decision on August 19, 1999, and denied a subsequent motion for reconsideration without opinion on September 13, 1999. The First Circuit's opinion, written by Judge Selya, affirmed the grant of summary judgment on several different grounds.

First, the First Circuit concluded that SMS had failed to demonstrate a genuine issue of material fact as to Digital's alleged monopoly power, regardless of how the relevant market was defined. Op. at 13A. SMS claimed that, for purposes of assessing monopoly power, the relevant market was the alleged aftermarket for servicing Digital mid-range servers and that the First Circuit could not consider the undisputed competition Digital faced in the primary equipment market. Op. at 8A. The First Circuit followed *Kodak*, however, and held that it was appropriate to take record evidence of primary market competition into account, and to assess the monopoly power issue in light of all the relevant facts in the record. Op. at 8A-12A.

Assessing all those facts, the First Circuit rejected SMS's contentions that this case was really just like *Kodak*. For example, SMS asserted that information costs in the alleged Digital service aftermarket had distorted market behavior just as they had in *Kodak*. Op. at 13A. The First Circuit disagreed and found *Kodak* to be fundamentally different on its facts: "The *Kodak* Court's discussion of information costs stemmed almost exclusively from the concern that the type of information necessary for allowing the primary market to check anticompetitive behavior in the aftermarket was unavailable to the average copy machine purchaser." Op. at 14A. Here, the record directly contradicted the existence of such "information deficits" in the alleged Digital service aftermarket. Op. at 14A. The warranty's existence was "obvious to any purchaser in the primary market." Op. at 14A. Moreover, the purely "prospective

nature of the warranty" undermined any analogy to the "bait and switch" tactics found to be problematic in *Kodak*. Op. at 15A-16A.

The First Circuit also held that SMS had failed to "create a genuine issue" as to the existence of an alleged "locked-in" customer base. Op. at 17A. Again relying on *Kodak*, SMS had attempted to draw an analogy "between the *Kodak* plaintiffs' need to buy copier parts and the perceived need of those who already own Digital computers to purchase any new hardware from Digital (rather than its competitors)." Op. at 16A. SMS asserted that such customers were "locked-in" to buying new hardware from Digital due to alleged "switching costs." Op. at 16A-17A. After reviewing the materials proffered by SMS, the First Circuit found that "SMS had not proffered significantly probative evidence sufficient to create a fact question as to whether this alleged switching cost is material to a large enough segment of Digital's installed base to harm competition." Op. at 18A. Moreover, review of the record afforded "no reason to believe that an appreciable number of Digital users are, in fact, significantly locked-in to making repeat purchases of Digital mid-range computers." Op. at 20A. Stating that "[a] lock-in phenomenon must be shown, not assumed," the Court determined that SMS had not made a sufficient showing to defeat summary judgment. Op. at 20A-21A, 24A.

After citing a number of other "empirical" shortcomings in SMS's case, Op. at 26A-28A, the First Circuit looked at the other required elements of SMS's Section 2 claim: lack of a legitimate business purpose and antitrust injury. On the first of these, the Court found, as an independent basis for summary judgment, that SMS had failed to produce evidence that Digital's warranty was anything other than "a legitimate sales tool." Op. at 30-31A. And, on the antitrust injury requirement, the Court determined that SMS had failed to establish *any* anticompetitive injury resulting from Digital's warranty. Op. at 33A.

REASONS FOR DENYING THE WRIT

Summary of Argument

The three "Questions Presented" asserted by SMS all go to the issue of whether summary judgment was appropriate on the unique record of this case. A writ of certiorari on any of these "Questions" is inappropriate here for three reasons.

First, there is no controversy concerning the appropriate summary judgment standards, and nothing about the way the First Circuit applied those standards is worthy of review. Not only did the First Circuit apply the right standards to the particular facts of this case, but the First Court's analysis was also entirely consistent with *Kodak,* in which this Court stated its preference "to resolve antitrust claims on a case-by-case basis, focusing on the particular facts disclosed by the record." *Kodak,* 504 U.S. at 467.

Second, this Court should not review this case because the Court cannot avoid becoming entangled in case-specific evidentiary issues. In applying the appropriate summary judgment standards, the First Circuit properly identified a series of gross deficiencies in the evidence proffered by SMS. These deficiencies included SMS's complete failure to come forward with admissible evidence of antitrust injury or exclusionary conduct. SMS's evidentiary failures on these points provide alternative grounds for summary judgment that are independent of the "Questions" raised by SMS in its Petition.

Third, the First Circuit's decision does not create or add to any circuit split. SMS does not identify any particular issue on which there is a split, nor is there any such issue. Each of the cases cited by SMS is entirely consistent with *Kodak,* with each other, and with the First Circuit's opinion. To the extent any of these cases vary in outcome, it is the result of the different facts of each particular case.

I. THE FIRST CIRCUIT CORRECTLY APPLIED WELL-ESTABLISHED SUMMARY JUDGMENT STANDARDS AND ITS DECISION DOES NOT CONFLICT WITH *KODAK*.

SMS's principal argument for certiorari boils down to the proposition that the First Circuit simply misapplied well-established summary judgment standards to the particular facts of this case. Not only is SMS wrong about this, but the issue itself is plainly not worthy of review by this Court.

A. The Summary Judgment Standards Are Well Established; No Important Federal Question Is Raised by Application of Those Standards to the Record Facts of this Case.

As SMS concedes, "numerous decisions of this Court focus on summary judgment standards." Pet. at 10 (citing, *e.g.*, *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986); *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986); *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 475 U.S. 574 (1986); and *Eastman Kodak Co. v. Image Technical Serv., Inc.*, 504 U.S. 451 (1992)). In cases such as *Matsushita* and *Kodak*, this Court has discussed and clarified the role of summary judgment in antitrust cases, and nothing that SMS raises in its petition creates any need for this Court to revisit the applicability of well-established summary judgment rules to the particular facts of this case.[7]

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7. It is well-settled that only issues of fact that are "genuine" and truly "material" will stave off summary judgment. *Celotex*, 477 U.S. at 325-27; *accord Springfield Terminal Ry. Co. v. Canadian Pac. Ltd.*, 133 F.3d 103, 106 (1st Cir. 1997). A "material" fact is one that "might effect the outcome of the suit." *Liberty Lobby*, 447 U.S. at 248. A dispute concerning a material fact is "genuine" only if "the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Id.* If the evidence proffered by the non-

(Cont'd)

SMS's argument that the First Circuit engaged in "judicial abuse of summary judgment," Pet. at 10, is based on distortions of the First Circuit's opinion. For example, the court did not "ma[k]e assumptions and weigh[ ] evidence." Pet. at 11. The First Circuit reviewed the record and determined that SMS had failed to create a genuine issue of material fact on the critical elements of its Section 2 claim. *See, e.g.*, Op. at 13A (SMS has not "managed to create a genuine issue of material fact as to [Digital's] alleged monopoly power"). Nor did the First Circuit base its decision "on the legal presumption that Digital's product warranty is 'pro-competitive' — indeed '*per se*' lawful." Pet. at 7. Rather, the court merely recited the undisputed record

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moving party is "merely colorable, or is not significantly probative, summary judgment may be granted." *Id.* at 249-50. Moreover, such evidence must be *admissible* if it is to be considered on summary judgment. Fed. R. Civ. P. 56(e).

While it is true that inferences must be drawn in favor of the non-moving party, such inferences must be justifiable. *Kodak*, 504 U.S. at 456 (citing *Liberty Lobby*, 477 U.S. at 255 and *Matsushita*, 475 U.S. at 587). On the other hand, unsupported assessments, conclusory allegations, and speculative suppositions carry no weight. *Liberty Lobby*, 447 U.S. at 249-50; *accord Springfield Terminal*, 133 F.3d at 106; *Medina-Munoz v. R.J. Reynolds Tobacco Co.*, 896 F.2d 5, 8 (1st Cir. 1990).

It is equally clear that summary judgment is no longer disfavored in antitrust cases. *Matsushita* teaches that courts should regard antitrust challenges to apparently competitive practices with a skeptical eye. 475 U.S. at 594. When an antitrust theory presents "a significant risk of deterring procompetitive conduct[,]" inferences should be drawn very carefully. *Kodak*, 504 U.S. at 478 (recognizing that mistaken inferences in antitrust cases "would be 'especially costly,' and would 'chill the very conduct the antitrust laws are designed to protect.' "); *see also Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 763 (1984) (refusing to infer concerted action when doing so would "deter or penalize perfectly legitimate conduct"). The First Circuit properly applied all these familiar standards in this case.

evidence establishing that warranties are generally used as "instrument[s] of competition" and that they tend to increase a "product's allure" in the eyes of consumers. Op. at 3A-4A. The First Circuit also did not simply "dismiss SMS's claims as 'less plausible' than [Digital's]." Pet. at 8. Rather, it reviewed the record and found the evidence allegedly supporting SMS's claims to be lacking. Op. at 34A ("Here, the record contains no significantly probative evidence that [Digital] is engaged in sinister practices or otherwise suffocating competition . . . .").[8]

Simply put, there is nothing about the First Circuit's application of the well-established summary judgment standards that raises any important issue of federal law or otherwise requires review by this Court.

B. The First Circuit's Decision — and Its Analysis of Section 2 of the Sherman Act — is Entirely Consistent with *Kodak* and Other Supreme Court Precedent.

There is equally no reason for the Court to grant certiorari to address what SMS vaguely describes as a "conflict" between the First Circuit's decision and *Kodak* "regarding summary judgment review." Pet. at 13. Not only is SMS again mischaracterizing the First Circuit's opinion, but in every particular the opinion is consistent with *Kodak* and is correct as a matter of law.

SMS asserts that the First Circuit's opinion is inconsistent with *Kodak* because it "fail[ed] to define a relevant market," and "ignored compelling evidence that Digital possessed monopoly power." Pet. at 9, 16, 17. This assertion grossly distorts what the First Circuit actually did. In reality, the First

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8. The First Circuit also did not "characterize[ ] SMS's theory as 'offbeat,' " as if to denigrate it, as SMS asserts. Pet. at 8. To the contrary, the court used the word "offbeat" only in a positive sense, as it expressly stated that "[t]here is . . . a certain offbeat logic to SMS's position." Op. at 4A.

Circuit correctly determined that — to survive summary judgment in a situation where Digital presented extensive record evidence to support its position — SMS had to demonstrate the existence of a genuine issue of material fact concerning Digital's alleged possession of "monopoly power in the relevant market." Op. at 7A (citing *United States v. Grinnell,* 384 U.S. 563, 570-71 (1966)). The court properly addressed the very essence of the summary judgment issue: whether there was sufficient evidence in the record to "support[ ] an inference of monopoly power *in the aftermarket* . . . ." Op. at 11A (emphasis added). On the record of this case, the First Circuit rightly concluded that SMS had *not* demonstrated any genuine issue of fact on the issue of monopoly power, no matter how the relevant market was defined. Op. at 12A-13A.

The First Circuit did not err in addressing the issue in this manner. Consistent with this Court's express statements in *Kodak*, the First Circuit recognized that, in assessing the possibility of monopoly power, it must consider the evidence of how competition in the primary equipment market influences the possibility of monopoly power in the aftermarket, including the evidence — if any — which "dissociat[es] the competitive situation in the aftermarket from activities occurring in the primary market." Op. at 11A. Indeed, this is what *Kodak* required when it mandated that courts conduct "a factual inquiry into the 'commercial realities' faced by consumers." 504 U.S. at 482.[9] *See also* 11A Areeda & Hovenkamp, *Antitrust Law*

9. As the First Circuit acknowledged, SMS's own

> theory depends on the proposition that [Digital] asserts power in the services aftermarket only by forcing matters in the primary computer equipment market . . . . This approach, in and of itself, invites us to look at the primary market, and thus tends to confirm our conclusion that, in determining whether [Digital] enjoys aftermarket monopoly, we cannot ignore the impact of the foremarket.

Op. at 12A n. 2.

¶ 531, at 156 ("Finding the relevant market and its structure is not a goal in itself but a surrogate for market power"); *Kodak*, 504 U.S. at 470 n.15 ("Whether considered in the conceptual category of 'market definition' or 'market power,' the ultimate inquiry is the same — whether competition in the equipment market will significantly restrain power in the service and parts market.").[10]

Moreover, in addressing the issue of monopoly power, the First Circuit actually did consider all of the evidence that SMS now claims it ignored. The court specifically noted and considered SMS's allegations that Digital had a high "share" of the alleged aftermarket, and that SMS contended that Digital's parts are "unique." Op. at 8A-9A. However, the First Circuit rightly concluded that this information, by itself, was insufficient to show "monopoly power." *Id.* at 9A. Rather, the court looked at the record as a whole and — as specifically required by *Kodak* — looked at the *evidence* as to whether Digital actually did have monopoly power in the alleged aftermarket: "As *Kodak* teaches, in aftermarket situations, market power *vel non* must be assessed by weighing the complete package of primary equipment, parts and services." Op. at 12A. Thus, the court properly focused on monopoly power, and — even assuming that the aftermarket could be a relevant market — correctly found that SMS had not "managed to create a genuine issue of material fact as to Digital's alleged monopoly power."

10. There is no requirement that the First Circuit, in analyzing monopoly power, first had to "shoehorn" Digital's warranty policies into the aftermarket, as SMS claims. *See Lee v. Life Ins. Co. of N. Am.*, 23 F.3d 14, 18 (1st Cir.) (rejecting plaintiffs' efforts to "shoehorn" their allegation into the "*Kodak* 'derivative aftermarket' model"), *cert. denied*, 513 U.S. 964 (1994). The "market definition" cases that SMS cites (such as *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962)) all had to do with defining what group or bundle of different products would fall within a single "relevant market" — *e.g.*, are rubber bands in the same relevant market as paper clips — not with the issue faced by the First Circuit here.

Op. at 13A. Far from acting inconsistently with *Kodak*, the First Circuit was doing precisely what *Kodak* envisioned and required.[11]

II. THE FIRST CIRCUIT RIGHTLY IDENTIFIED A NUMBER OF WAYS IN WHICH SMS FAILED TO PRODUCE SUFFICIENT EVIDENCE TO SUPPORT SEVERAL ESSENTIAL ELEMENTS OF ITS SECTION 2 CLAIM.

This case is also not an appropriate candidate for certiorari review because the First Circuit properly identified a number of ways in which SMS failed to produce sufficient evidence to meet its summary judgment burden on critical elements of its Section 2 claim. Op. at 13A-26A. If this Court were to grant certiorari, it could not avoid entangling itself in these fact-specific issues, which are of no importance beyond this matter.

A. SMS Failed to Present Evidence of the Supposed "Lock-In."

The first of these evidentiary failures relates to SMS's supposed "lock-in" theory, which was pivotal to SMS's theory of liability. The First Circuit rightly held that the "evidence" of lock-in or switching costs proffered by SMS was not sufficient to create a genuine dispute of fact as to "whether this alleged

11. SMS also argues that the First Circuit improperly "conditioned any finding of aftermarket monopoly power on proof of a change in policy, a holding never adopted by this Court." Pet. at 9. As discussed in more detail below, SMS mischaracterizes the First Circuit's holding. *See infra* 21.

Likewise unconvincing is SMS's claim that the First Circuit made a "determination that warranties are 'pro-competitive' . . . and pave[d] the way for *per se* legality which has been condemned by this Court." Pet. at 10. The First Circuit did no such thing. It merely recited the "general experience" that warranties are "tools of competition" and that they tend to increase a "product's allure." Op. at 3A-4A (citing 3A Areeda & Hovenkamp, *Antitrust Law* ¶ 761, at 55).

switching cost is material to a large enough segment of [Digital's] installed base to harm competition." Op. at 18A. Simply put, SMS's evidence gave "*no* reason to believe that an appreciable number of [Digital] users are, in fact, significantly locked-in to making repeat purchases of Digital mid-range computers." Op. at 20A (emphasis added).

The First Circuit's conclusions on this point do not raise any important issue of law, but are based on specific evidentiary deficiencies. The only evidence proffered by SMS was the testimony of individuals employed by *two* of Digital's many thousands of customers. These individuals gave their opinions that it can be costly to migrate to a different platform once a company has committed to a certain brand of hardware and has acquired ancillary software. But this testimony was neither admissible nor probative. Op. at 21A. These individuals did not have the personal knowledge or experience necessary to testify about how companies decide to purchase new computer hardware; none of them bore the ultimate responsibility for making such a decision; and none of them had any specific or detailed knowledge about how management might calculate switching costs. *Id.* None of them, therefore, could or did testify about the ultimate issue — "the nature of a company's decision to purchase new computer hardware." Op. at 21A. *See Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579, 592 (1993) (requirement of first-hand knowledge represents the "common law insistence upon 'the most reliable source of information' "); *accord Acosta-Mestre v. Hilton Int'l of Puerto Rico*, 156 F.3d 49, 57 (1st Cir. 1998) (district court properly excluded testimony not based on personal knowledge).[12]

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12. The First Circuit also properly determined that, even were the individuals' testimony admissible, SMS's paltry showing was insufficient to even raise a question of fact that "consumers are generally worse off as a result of DEC's warranty policy." Op. at

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Moreover, the First Circuit found that SMS had failed to produce any evidence that accounted for the "complex nature of the decision to purchase a new computer system." Op. at 22A. According to the court, the record showed that the "availability of software applications designed to meet current or anticipated business needs usually is the determinative factor in choosing whether to buy a new computer." *Id.*[13] But SMS had offered no evidence whatsoever that took "into account the efficiency gains of buying new software — gains that often may dwarf hardware price in dollar terms." *Id.*

In short, after reviewing and considering all the evidence in the record, the court concluded that "[a] lock-in phenomenon must be shown, not assumed," and that SMS had not made the necessary showing. Op. at 20A-21A, 24A. There is no reason for this Court to review this case-specific conclusion.

B. SMS Failed to Rebut Undisputed Evidence of Digital's Legitimate Business Interest in Adopting the Warranties.

SMS also failed to provide any evidence that raised a genuine dispute of material fact on another critical element of its Section 2 claim. Consistent with *Kodak*, the First Circuit

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19A. *Liberty Lobby*, 477 U.S. at 249-50 ("If the evidence is merely colorable, or is not significantly probative, summary judgment may be granted.") (citations omitted); *Matsushita*, 475 U.S. at 586 (summary judgment opponent "must do more than simply show that there is some metaphysical doubt as to the material facts").

13. SMS offered a marketing survey and report which confirmed that "[software] 'applications drive the choice of platforms . . . .' " Op. at 22A. In fact, each of the witnesses proffered by SMS acknowledged that, "all things considered, if a new computer system would bring more benefits, there would be no objection to the switch." Op. at 24A.

correctly noted that, "to make out a Section 2 claim, the plaintiff must show that the alleged monopolist has engaged in improper exclusionary conduct." Op. at 30A (citing *Kodak,* 504 U.S. at 482-83; *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 600-05 (1985)). As stated above, SMS asserted that the inclusion of a three-year warranty on new equipment constituted such "improper conduct." Op. at 31A. Digital, however, provided overwhelming evidence of its legitimate business interests in adopting the warranty. Op. at 3A-4A, 31A. As this Court recognized in *Aspen Skiing,* 472 U.S. at 605, "valid business reasons" are a defense to a Section 2 claim.[14]

In response to Digital's evidence, SMS offered only two internal Digital documents, neither of which provided any evidence of improper conduct. Op. at 31A ("neither document so much as hints at an intent to suffocate the aftermarket"). Moreover, the First Circuit rightly found that SMS's unsupported assertion that Digital adopted its warranty for anticompetitive purposes "defies common sense." Op. at 32A. The only evidence in the record fully documented that Digital's warranty was simply a legitimate sales tool which Digital properly used as a means of growing market share in the primary market. Op. at 30-31A.

Thus, there was no evidence in the record to support the "exclusionary conduct" element of SMS's Section 2 claim, and

14. The record evidence established that Digital's motive in adopting the warranties was "to promote the sales of its new Alpha computers." Mem. at 36A. It was undisputed that Digital's products were competing against other manufacturers' computers with three-year warranties. Mem. at 39A n.2 (acknowledging warranty terms of Compaq and IBM). It was also undisputed that, by 1997, potential computer customers had a strong preference for a three-year warranty. SA87. Digital's desire to promote sales, satisfy its customers, and beat or match its competitors constitutes a legitimate, pro-competitive business purpose. *Grappone, Inc. v. Subaru of New England, Inc.*, 858 F.2d 792, 799 (1st Cir. 1988) (policy adopted for the "procompetitive purpose of helping the firm develop or maintain sales" is a legitimate purpose).

the lack of such evidence provides a basis for summary judgment that is independent of the First Circuit's monopoly power analysis. SMS provides no reason for the Court to review the First Circuit's conclusions on the "exclusionary conduct" issue.

C. SMS Failed to Provide Any Evidence of Another Essential Element of Its Claim: Antitrust Injury.

The First Circuit also correctly held that SMS had failed to come forward with any evidence of the required "antitrust injury," i.e., injury to competition, rather than injury to competitors. Op. at 33A. Such a failure provides another basis for dismissing SMS's antitrust claim. *See Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 458-59 (1993).

As recounted above, Digital produced undisputed evidence that competition is unaffected by its warranties, and that SMS and other service providers are competing vigorously for service business on Digital computers sold with three-year warranties. *See* Op. at 32A ("ISOs are free to service all [Digital] computers, including those under warranty, both during the warranty period and after its expiration."); SA38-41. As the First Circuit observed: "[Digital] has placed no restriction on the aftermarket for service of its products. Parts are available to all market participants, and there is no indication in the record either that there are restrictions on their availability or that such a policy is even being contemplated." Op. at 32A.

SMS, the record shows, failed to come forward with any admissible evidence of either a reduction in the supply or quality of service or an increase in service prices as a result of Digital's three-year warranties. The only "evidence" SMS proffered on this issue, aside from the "self-serving speculation" of an SMS employee, *see* Op. at 28A,[15] was the affidavit of SMS's retained

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15. SMS's director of marketing stated that: "It has been my experience that when [Digital] does not face competition, its prices tend to be higher . . . Thus, the elimination of competition from SMS

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expert. Op. at 28A, 29A. The First Circuit correctly disregarded the expert's conclusions as inadmissible and "deficient on several levels." Op. at 29A-30A (citing *Kumho Tire Co. v. Carmichael*, 526 U.S. 137, 119 S. Ct. 1167, 1179 (1999) ("nothing . . . requires a district court to admit opinion evidence that is connected to existing data only by the ipse dixit of the expert")).

Finally, as the First Circuit correctly stated, "the record is devoid of any evidence of supracompetitive prices or other oppressive terms of business in the aftermarket." Op. at 26A. SMS produced "no evidence that [Digital] has displayed a pattern of raising service and parts prices in the aftermarket, nor is there evidence that the price of the warranty itself represented a means of extracting monopoly profits." *Id.* at n.5. SMS's complete lack of evidence on this issue led the court to properly conclude that "there is no objective indication of harm to competition . . . ." Op. at 26A, 33A. This, too, is not an issue worthy of review by this Court, and — indeed — SMS does not even raise or discuss antitrust injury in its Petition.

III. THERE IS NO CIRCUIT SPLIT; THE FIRST CIRCUIT'S OPINION IS CONSISTENT WITH THE OTHER CIRCUIT COURT CASES ON AFTERMARKET ISSUES AND WITH *KODAK*.

Finally, this Court should reject SMS's contention that certiorari is needed to "resolve a growing split among the circuits regarding the evidence necessary to establish monopoly power in an aftermarket." Pet. at 20. There is no such split, and nothing in the First Circuit's decision creates or contributes to any split.

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and other Independent Service Organizations, *should* result in price increases to customers." Op. at 28A (emphasis added). As the First Circuit correctly noted, such an unsupported opinion is "conclusory conjecture," Op. at 28A, which is rightly ignored on summary judgment. *Liberty Lobby*, 447 U.S. at 249-50.

SMS never identifies — either in its "Questions Presented" or in the body of its Petition — precisely what legal issue is supposedly in dispute among the circuits. This is telling, for there is *no* circuit split on any issue raised by this case. SMS is thus reduced to making a general attack on the direction that certain courts, in various different factual contexts, have taken in post-*Kodak* decisions involving an alleged aftermarket. *See* Pet. at 21-22.

Moreover, SMS's entire argument concerning a supposed circuit split is flawed because it is premised on a mischaracterization of the First Circuit's opinion. SMS asserts that the First Circuit held that evidence of a lock-in "will not allow for a finding of aftermarket monopoly power unless it is also accompanied by proof of a policy change." Pet. at 21 (citing Op. at 15A-16A). SMS terms this a "policy change limitation." The First Circuit adopted no such limitation.

Instead, at Op. at 15A-16A, the court focused on two undisputed facts which make Digital's warranty situation substantively different from *Kodak* and from other recent aftermarket cases. The first fact is that Digital's warranty is "transparent" (or known) to buyers of computers in the primary equipment market. Op. at 14A-15A. The second fact is that Digital's warranty is "prospective," in that it only applied to purchases of new computers. Op. at 15A. The First Circuit did not focus on these two facts as evidence of the existence or non-existence of a "policy change," as SMS asserts. Rather, the First Circuit focused on the importance of the "transparent" and "prospective" nature of Digital's warranty because it made Digital's warranty fundamentally different from the "bait and switch" tactics that this Court found to be predatory in *Kodak*. Op. at 15A-16A. Nowhere in the First Circuit's discussion, or anywhere else in the opinion, did the Court adopt a holding requiring a "policy change limitation."

When the First Circuit's opinion is read without the distortion imposed upon it by SMS, the opinion clearly does not conflict with any other Court of Appeals case, or with *Kodak* or other decisions of this Court.[16] Indeed, the First Circuit's opinion is entirely consistent with *Kodak* in that it examined

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16. SMS cites three circuit court opinions as examples of the supposedly "correct" role of evidence of "policy change" in a post-*Kodak* analysis of market power in an alleged aftermarket. Pet. at 22. None of these cases even discuss policy changes, however, for a simple reason: there was no evidence of any policy change before the courts. Rather, the cases presented other facts from which the courts determined that plaintiffs had presented sufficient evidence of market power for summary judgment purposes. *See, e.g., Datagate, Inc. v. Hewlett-Packard Co.*, 60 F.3d 1421 (9th Cir. 1995) (evidence concerning dollar volume of contract was sufficient to preclude finding on summary judgment that tying arrangement affecting only one customer was "insubstantial" and did not have a sufficient impact on competition), *cert. denied*, 517 U.S. 1115 (1996). Put simply, none of these cases creates any "circuit split" when they do not discuss, consider or adopt the so-called "policy change" limitation that SMS contends is erroneous.

As for *Red Lion Med. Safety, Inc. v. Ohmeda, Inc.*, 63 F. Supp. 2d 1218, 1229-1232 (E.D. Cal. 1999), a recent district court case which came out only days before the First Circuit's decision, that case is clearly factually distinct from the present case. *Red Lion* involved restrictive parts policies imposed on an alleged aftermarket; no warranty was involved. Moreover, far from "rejecting the policy change limitation on market power" as alleged by SMS, the district court simply determined that evidence of a policy change was not the *only* evidence which would permit an inference of market power in an aftermarket on summary judgment. *Id.* at 1230-31.

Finally, SMS's assertion of a "conflict" involving various aftermarket cases ignores the fact that each of the cases was addressing unique factual circumstances and different evidentiary records. Each of the courts appropriately reviewed the unique facts in its record and applied *Kodak* to those facts. That there was a different result in the cases based on the facts presented does not create a "split" in the circuits. The findings and results in each of the aftermarket cases cited by SMS are entirely consistent with the First Circuit's opinion, as well as with the other circuit court opinions attacked by SMS.

the evidence actually in the record in order to determine what evidence, if any, there was of an impact of the warranty on consumers. Certainly, the First Circuit itself did not recognize that its decision conflicts with any other Court of Appeals decision; to the contrary, it recognized that it is consistent with and in tune with the general consensus among all the courts which have considered aftermarket issues. *See, e.g.*, Op. at 15 (citing as "accord" with *PSI Repair Serv. Inc. v. Honeywell, Inc.*, 104 F.3d 811, 819-820, 822 (6th Cir.), *cert. denied*, 520 U.S. 1265 (1997)); Op. at 16A (citing *Digital Equip. Corp. v. Uniq. Digital Tech., Inc.*, 73 F.3d 756, 763 (7th Cir. 1996)).

The First Circuit's opinion also does not create or add to any circuit split because it is the *only* case to address directly the alleged anticompetitive impact of a warranty policy.[17] Warranties are different from the various other alleged aftermarket practices (such as restrictive spare parts policies) which are discussed in *Kodak* and the other cases relied upon by SMS. As the First Circuit rightly noted, there was extensive *evidence* in the record of the legitimate, pro-competitive purposes of Digital's equipment warranties, and of the fact that those warranties were both transparent and prospective. Op. at 3A-4A, 13A-16A, 30A-31A. The only other circuit court decision to touch on warranty issues in a similar antitrust context is *Marts v. Xerox, Inc.*, 77 F.3d 1109, 1112 (8th Cir. 1996). The First Circuit here expressly agreed with the Eighth Circuit in concluding that, "as long as a warranty does not limit a customer's choice of service provider, there is usually no antitrust problem." Op. at 19A, (also citing *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 12 (1984)).

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17. SMS does not cite, because it cannot, any other case in which a warranty has been challenged on antitrust monopoly grounds. The factual context of this case is unique; and there is no groundswell of similar or related cases that would make it important for this Court to address this type of fact pattern.

In short, there is nothing about this case that makes it worthy of this Court's review. Even if there were a circuit split on some discrete, identifiable issue — which there is not — this case still would not be a good vehicle to resolve or address that issue, because of all the case-specific factual reasons stated above, and because of the alternative grounds the First Circuit gave for its decision.

CONCLUSION

For the foregoing reasons, respondent respectfully requests that this Court deny the petition for writ of certiorari in this case.

Respectfully submitted,

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